

**MINUTES
of the
FOURTH MEETING
of the
INVESTMENTS AND PENSIONS OVERSIGHT COMMITTEE**

**September 5, 2007
State Capitol
Santa Fe**

The fourth meeting of the Investments and Pensions Oversight Committee for the 2007 interim was called to order by Senator John Arthur Smith, chair, on Wednesday, September 5, 2007, at 10:15 a.m. at the State Capitol in Santa Fe.

Present

Sen. John Arthur Smith, Chair
Rep. Donald E. Bratton
Rep. Larry A. Larrañaga
Sen. Carroll H. Leavell
Sen. Mary Kay Papen
Rep. Henry Kiki Saavedra
Rep. Jim R. Trujillo
Rep. Luciano "Lucky" Varela

Absent

Rep. John A. Heaton, Vice Chair
Sen. Joseph J. Carraro
Sen. Phil A. Griego

Advisory Members

Sen. Carlos R. Cisneros
Robert Gish, Public Employees Retirement
Association (PERA)
Bob Jacksha Educational Retirement Board
(ERB)
Adam Levine for Gary Bland, State
Investment Council
James Lewis, State Treasurer
Rep. Patricia A. Lundstrom
Olivia Padilla-Jackson, Board of Finance
Rep. John Pena
Rep. Jane E. Powdrell-Culbert
Sen. Leonard Lee Rawson
Rep. Sheryl Williams Stapleton

Rep. Andrew J. Barreras
Sen. Pete Campos
Rep. Miguel P. Garcia
Sen. Stuart Ingle
Sen. Michael S. Sanchez
Sen. H. Diane Snyder
Rep. Eric A. Youngberg

Staff

David Abbey, Legislative Finance Committee (LFC)
Michelle Aubel, LFC
Cleo Griffith, Legislative Council Service (LCS)
Larry Matlock, LCS
Wayne Probst, LFC

Stephanie Schardin, LFC
Doug Williams, LCS

Guests

The guest list is in the meeting file.

Wednesday, September 5

The committee adopted the minutes of the August 14, 2007 meeting.

New Mexico State Firefighters Association (NMSFFA); Retirement

—Ronnie Walls, Secretary/Treasurer, NMSFFA

—Vernon Muller, Deputy State Fire Marshal

There are approximately 6,500 volunteer firefighters in New Mexico; however, the PERA database contains 16,000 names of volunteer firefighters. PERA initiated a process in an attempt to purify its database. The deadline for responses has passed and only 222 of 367 volunteer fire departments responded to the PERA questionnaire.

The PERA maintained that the Volunteer Firefighter Retirement Fund has a current balance of approximately \$43 million. The annual new revenue to the fund is \$750,000, and the annual payout is \$450,000.

Approximately 350 firefighters are currently receiving retirement benefits.

Mr. Walls suggested that the PERA database might be examined for entries with no activity for over two years. Names with no activity could be transferred to an inactive list. In this way, the actuary might be able to provide a more accurate estimate of the impact of an improvement in retirement benefits.

Mr. Muller suggested that database purification might be accomplished by the Office of the State Fire Marshal working through local governments.

Representative Varela asked if fire chiefs can be informed of the fact that the volunteer benefit does not affect other retirement benefits. Mary Frederick, PERA, responded that such a notification could be mailed.

Senator Leavell asked if legislation is required to purify the database. Mr. Muller responded that he will consult legal counsel at the Office of the State Fire Marshall's Office.

Senator Papen asked if individual firefighters can self-identify to the PERA rather than depending upon the local fire chief. Mr. Slattery, PERA, responded that current law requires certification by the fire chief.

Senator Rawson asked if volunteer firefighters are covered by workers' compensation. Mr. Muller said that he would investigate workers' compensation eligibility.

Senator Rawson suggested imposing an annual filing fee to be submitted by volunteer firefighters as a way of annual certification of active status.

Representative Trujillo suggested legislation requiring local governments to file the necessary annual certification. Mr. Muller said that the Office of the State Fire Marshal's Office is investigating the need for legislation.

Senator Smith suggested examining volunteer firefighter practices in other states. He noted that the legislature wants to help, but does not know how to proceed. Senator Smith requested staff to research the issue and indicated that model legislation may be needed. He also noted that the New Mexico Municipal League and New Mexico Association of Counties should be involved.

New Mexico Retiree Health Care Authority (NMRHCA); Update

- David Abbey, Director, LFC
- Katherine Miller, Secretary, Department of Finance and Administration
- Marie Thames, Executive Director, NMRHCA
- Danielle Wilson, Chair, NMRHCA Board

Two major issues were discussed:

- the solvency period has declined from 25 years in FY06 to nine years in FY08; and
- as the result of a recent reporting requirement, GASB 45, the state has a \$5 billion unfunded accrued actuarial liability (UAAL).

The factors affecting solvency include:

- the rising costs of health care and increasing membership;
- overly generous service and eligibility requirements, benefits packages and subsidies;
- premium increases have not kept up with rises in health care costs;
- the relatively young age of retirees;
- membership is expected to increase 7% to 8% per year;
- claims costs are expected to increase at 8% to 20%+ per year; and
- expenditures are outpacing revenue streams.

Additional factors involving the amount and type of subsidy include:

- premium subsidies provided to retirees, spouses and dependents are applied without a clear correlation to the underlying, true cost or to the amount an individual paid into the system;
- younger retirees receive a greater subsidy than Medicare-eligible retirees; and
- the amount of the subsidy applied by years of credible service is established in an administrative rule, but implemented by the Board of Directors.

Finally, the system was not adequately funded at inception; therefore, all of the active employer/employee contributions are being spent to provide benefits to the retirees and their families.

The work group considered numerous options and will recommend those that are deemed to have the greatest impact on the solvency of the fund and that raise the greatest amount of revenue. Possible work group recommendations include:

Action	Savings (in millions)	Additional Solvency (in years)
A fully insured Medicare benefit	\$4.0	2.0
Decreasing retiree and spouse subsidy by 10%	\$14.0	7.0
Implementing age and service: rule of 70 for public safety, rule of 80 for all other retirees	\$6.0	3.0
Increasing contributions: active employee 0.05%, employer 0.10%	\$4.0	2.0
Maintaining general fund appropriation	\$3.0	1.5
Subtotal, including changes already made by the NMRHCA board	\$38.6	19.1
Existing solvency period		9.0
Total solvency if all recommendations are implemented		28.1

Other potential recommendations include:

- adopting effective disease management;
- contracting with fewer carriers;
- attestation regarding other coverage;
- implementing a statewide formulary;
- consolidating administrative functions (GSD, PSIA, RHCA);
- consolidating "pools"; and
- rebalancing board composition.

Mr. Abbey suggested that increasing active employee/employer contributions diverts available funds that might be directed toward salaries. New Mexico state government already has a high benefit overhead of approximately 39%, and this places the state at a competitive disadvantage compared to other employers.

Ms. Miller noted that a multipronged approach is needed to solve the problem. It will require participation by retirees, active employees, the legislature and the NMRHCA board.

Representative Bratton asked about the savings associated with implementation of the rule of 80. Mr. Abbey responded that the rule of 80 would result in a \$6 million annual savings.

Representative Bratton asked if retirees who return to work are required to use health care coverage provided by a new employer rather than RHCA benefits. Ms. Thames responded that there is currently such a requirement.

Senator Smith asked about the working group's recommendations concerning the composition of the NMRHCA board. Mr. Abbey responded that the group has discussed greater representation by state officials such as the secretary of finance and administration.

Representative Varela requested Mr. Abbey to obtain the most current NMRHCA financial reports.

Representative Varela stated that he wants retirees to be informed about the working group's recommendations before the legislature takes any action. Ms. Wilson responded that the NMRHCA will use its periodic newsletter to keep retirees informed.

State Treasurer's Office; Proposed Legislation

—James Lewis, State Treasurer

The Local Government Investment Pool (LGIP) was established by the legislature in 1988. The LGIP has a current market value of \$1 billion. As of August 31, 2007, the LGIP had a gross yield of 5.3748% and a weighted average maturity of 31 days. The LGIP has a Standard & Poors rating of AAAm.

Currently, participants in the pool include:

- 42 cities, towns and villages;
- four judicial districts;
- 18 counties;
- 39 school districts;
- 16 special districts;
- eight universities and colleges; and
- eight quasi-governmental agencies.

The proposed 2008 LGIP legislation would:

- allow direct participation by Indian pueblos and tribes and other new participants (such as the Renewal Energy Transmission Authority, a newly created quasi-governmental agency) without having to amend the statute each time a new entity wants to invest in the fund;
- create a medium-term fund (maximum 3-year maturity) for eligible governing bodies to invest bond proceeds of local bond issues. Arbitrage rebate calculation services will be offered to participants;
- eliminate the 181-day maximum investment term for participating entities, allowing

- longer investment periods at their discretion;
- extend the state treasurer's maximum portfolio maturity from 13 months to three years;
- allow enhanced local government investment services; and
- allow the state treasurer to invest the general fund in the LGIP for liquidity management purposes. The general fund investment would be limited to no more than 5% of the LGIP fund market value.

Senator Smith noted that, last year, this legislation passed the House and was voted favorably by the Senate Finance Committee but failed to pass the Senate because of time considerations. He also stated that the legislation was not controversial.

Investment Performance Update; June 30, 2007 Quarterly Reports

—Bob Jacksha, ERB
 —Robert Gish, PERA
 —Adam Levine, State Investment Council (SIC)

Mr. Jacksha reported the ERB investment results as follows.

- Over the last 12 months, the fund experienced a gross investment gain of \$1.4 billion, easily outpacing the \$146.1 million in net distributions. The fund recorded a gross investment gain of \$348.0 million for the quarter. Total assets increased from \$9.1 billion at the beginning of the quarter to \$9.4 billion, with \$26.3 million in net distributions.
- Over the past five years, the fund returned 11.5% per year, beating its policy index by 0.1% and ranking in the thirtieth percentile of the Independent Consultant Cooperative's Public Funds Universe.
- For the year, the fund returned 17.6%, trailing its policy benchmark by 0.3% and ranking in the thirty-fourth percentile of public funds.
- For the quarter, the fund posted a 3.9% return, beating its policy index by 0.4% and ranking in the fifty-second percentile of public funds.
- Total equity exposure was 61.1%, which is above the target by 3.1% and under the upper limit of 63%. This exposure is higher than the first quarter and can be attributed to a strong quarter for both domestic and international equities. An additional \$330 million was funded to hedge fund managers, bringing hedge fund exposure to 8.2%, which is 3.2% over its current target. Private equity continues to be underweight relative to its target as the program is implemented.

A summary of market value for fiscal year 2007 is as follows:

Beginning market value	\$8,167,083
Net external growth	-146,068
Return on investment	1,418,112
Income received	181,163
Gain/loss	1,236,949
Ending market value	\$9,439,127

Senator Smith asked about ERB's accrued liability. Mr. Jacksha responded that it stands at \$3.6 billion and is expected to decline.

Representative Larrañaga asked about the return on investment compared to the ERB 8% benchmark. Mr. Jacksha stated that total annual return was 17.6%, or 9.6% over the benchmark.

Representative Larrañaga asked how the PERA's assets may be invested in alternative investments. Mr. Gish stated that the board policy is to permit 5% in hedge funds, 5% in private equity and 5% in real estate.

Representative Bratton expressed concern over sub-prime lending investments.

Representative Larrañaga noted that there are differences in the asset allocations for the Land Grant and Severance Tax Permanent funds. Mr. Levine responded that, for the most part, the two funds have identical asset allocations; however, the Severance Tax Permanent Fund (STPF) was designated by the legislature for participation in the New Mexico private equity program.

Mr. Levine reported the SIC investment results as follows.

- Over the last 12 months, the combined funds experienced a net investment gain of \$2.4 billion with \$924.8 million coming in the quarter. Net contributions totaled \$86.3 million for the year. Total assets increased from \$15.1 billion at the beginning of the quarter to \$16.1 billion at quarter end with \$31.2 million in net contributions.
- Over the past five years, LGPF returned 11.1% per year, outperforming its policy index by 0.3% and ranking in the forty-sixth percentile of the Independent Consultant Cooperative's Endowments and Foundations Universe. Over the same period, STPF returned 10.9% per year, lagging its policy index by 0.2% and ranking in the fifty-fourth percentile.
- For the year, LGPF returned 17.9%, outperforming its policy index by 0.6%, while the STPF returned 17.8%, performing in line with its policy. For the quarter, LGPF returned 6.1%, surpassing its policy return by 1.5%. Over the same period, STPF outperformed its policy index by 1.7%, with a return of 6.5%.

A summary of market value for fiscal year 2007 is as follows:

Beginning market value	\$13,624,701,792
Contributions	786,043,211
Distributions	-699,752,306
Net transfers	86,209,905
Fees	-18,183,332
Income	438,233,259
Capital appreciation	1,973,577,975
Net investment gains	2,393,627,902
Ending market value	\$16,104,620,599

Mr. Gish reported that the PERA's fiscal year 2007 investment return was 18.08% compared to a benchmark of 16.71%.

In-Depth Examination of Equity Strategies

—Gary Bland, SIC

This agenda item was postponed until the October 17, 2007 meeting.

Discussion of Agenda Items for the October 17, 2007 Meeting

- **State Fire Marshal; Retirement**
—Vernon Muller, Deputy State Fire Marshal
- **Department of Public Safety, Motor Transportation Division; Retirement**
—Lt. Colonel Mark C. Rowley
- **Other**

Other Business

There was no other business brought before the committee.

The committee adjourned at 4:00 p.m.